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Mayra Y Ahern 07/24/2006 09:47:16 AM From DB/Inbox: Mayra Y Ahern

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DISSEMINATION: ECON
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APPROVED: ECPO:CHILL-HERNDON
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C O N F I D E N T I A L SECTION 01 OF 02 CAIRO 004518

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NEA FOR ELA

E.O. 12958: DECL: 07/20/2016
TAGS: [ENRG](#) [ECON](#) [PGOV](#) [EG](#)
SUBJECT: EGYPT: IMMINENT INCREASE IN GASOLINE PRICE?

Classified By: Counselor for Economic and Political Counselor Catherine Hill-Herndon for reasons 1.4 (b) and (d).

Summary

1. (C) The Egyptian Cabinet has apparently approved an increase in the heavily-subsidized gasoline price, although specifics regarding the extent of the increase were not given. The Minister of Petroleum believes an announcement could come within days, although fears over domestic turbulence amidst regional turmoil could delay Presidential approval. End Summary.

Price Increase on the Way

2. (C) During a July 20 meeting with visiting U.S. Secretary of Energy Bodman (memcon septel), Egyptian Minister of Petroleum Sameh Fahmy, in response to a query by the Secretary, said the Egyptian cabinet had approved an increase

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in the gasoline price, likely within "the next several days or next week." Fahmy did not specify the size of the imminent increase. Post, AmCham, and the major players in the downstream market here, led by ExxonMobil, have long been pressing for a move toward more realistic pricing of petroleum products in Egypt.

3. (SBU) According to recent meetings with industry sources, plans were reportedly afoot in the Cabinet to raise the price of 90 octane fuel from LE 1 (17 cents) to LE 1.30 (USD 23 cents) per liter, thereby making it just slightly less expensive than the higher grade 92 octane that retails for LE 1.40. While this move would only negligibly affect the

overall subsidy, it would be a major boost to downstream retailers. Exxon-Mobil, in particular, has plans to invest an additional USD 100 million in Egypt over the next 6-7 years to upgrade service stations and other aspects of its retail business. This plan, however, was based on an assumption that the GOE will reduce the subsidy and move to more reasonable pricing.

Cheap Gas, Zero Margins

14. (SBU) Gasoline prices in Egypt are five to seven times lower than comparable markets in the region, placing gasoline here among the cheapest in the world. A liter of 90 octane gasoline costs LE 1 (USD 17 cents). Official GOE estimates place the cost of the subsidy at LE 40 billion per year (USD 7 billion), although these estimates were made at a time of USD 50 per barrel oil. Fuels costs are set nationally, and the price of 90 octane gasoline has remained static for fourteen years. The GOE did, however, increase the price of diesel fuel in 2004 by nearly 50 percent with negligible flow-through effects on the costs of services. In the absence of market pricing, and with all possible efficiencies exploited, downstream retailers require a margin increase to squeeze any profitability from their retail operations. The price increase will create space for such an increase. In addition, the increase should help ease some of the spot shortages felt by retailers who continually fight to supply the market.

Preparing the Public?

15. (SBU) If enacted, the price increase will make good on a steady, and public, drumbeat from senior GOE officials on the need to reduce gasoline subsidies. On May 24, Fahmy stated before the Industry Committee of the People's Assembly, for the first time publicly, that subsidies "are a real pressure" on the GOE and that "no one would guarantee the stability of prices" for the indefinite future. Minister of Finance Yousef Boutros Ghali has also been quoted decrying the subsidy as benefiting primarily the wealthiest tier of Egyptians and suggesting the money could better be spent on education, social services, etc. Other senior officials, including the Minister for Social Insurance, have weighed in publicly on the subject.

Possible Flow-through Effect

16. (C) The actual impact of an increase in the fuel price is likely to have a negligible financial effect on the average consumer according to industry sources. Following the doubling of diesel prices in 2004, ExxonMobil did a study on the flow-through effect of the increase on their large fleet of diesel powered trucks. The study found that the 50 percent increase in fuel costs only translated into a 5 percent increase in transport costs. Granted ExxonMobil's transportation operations run with greater efficiencies than most, but contacts tell us that even the most inefficient operations would likely see an increase of 10 percent on average. Price gauging at the consumer level, however, could impact those with a less than sophisticated understanding of the effects of commodity price changes. In 2004, complaints erupted among the many, mostly lower-income Cairenes who rely on the city's ubiquitous mini-bus taxis over price gauging. Many drivers, it appears, took the 50 percent increase in diesel price as license to increase their fares by fifty percent as well.

Comment

17. (C) Despite the Cabinet's apparent approval of the

measure, President Mubarak could be disinclined to ok any move that could cause domestic turbulence, particularly given other events in the region. Even though the effect of the price increase on the average Egyptian would likely be negligible, price gauging and resentment at the removal of an entitlement could spark dissent among the masses. If enacted, the price increase could have a significant and positive impact on downstream companies' profitability with only minor flow-through effects on the driving public.

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